

# 2021: THE BIDEN TAX PLAN

WHAT EVERY  
BUSINESS OWNER  
THINKING ABOUT  
SELLING  
NEEDS TO KNOW NOW

## OVERVIEW:

“*Biden's proposed tax changes may drive negative tax consequences for business transactions in 2022 and beyond.*”

The incoming Biden administration's proposed tax changes represent a significant change in tax policy that will impact long-term capital gains for business owners.

These changes can really impact those that are thinking about selling within the next few years, and may drive negative tax consequences to sales in 2022 and beyond.

While nothing is final yet, **these potential changes should cause small to midsize business owners thinking about selling their business within the next five years to consider accelerating their plans.**



## THE PLAN'S KEY POINTS:

Biden's proposed tax plan will have a broad impact on business owners and should be evaluated as owners consider the timing of exiting their businesses. Certain pieces of the proposed plan would merely reverse components of the Tax Cuts and Jobs Act of 2017, yet other pieces of the proposal are new.

Biden's proposal adds new tax obligations and removes some tax benefits. The plan includes:

- Essentially doubling the tax rate on material long-term capital gains from 20% to 39.6% (for those with adjusted gross income (AGI) exceeding \$1million)
- Raising the top individual tax rate from 37% to 39.6%
- Adding a new 12.4% high-earner payroll tax on income above \$400,000
- Eliminating the qualified income deduction for partnerships and S corporations

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## CONSIDER THIS EXAMPLE

Biden's proposed tax plan would effectively double the long-term capital gains tax from 20% to 39.6%. To achieve the same net proceeds of a sale in this scenario, **a business owner would require a 32% higher sale price.** This alone is a reason for potential sellers to accelerate their sale plans if possible.

Consider this example. Assume a company is sold, and the owner's net proceeds is \$5m with no debt.

Timing of Sale	Seller's Taxable Proceeds	Tax Basis	Taxable Gain	Top Fed Tax Rate	Cap Gains Tax	After Tax Proceeds
Pre-Biden Plan	\$5m	\$0	\$5M	20%	\$741,960	\$4.26m
Post-Biden Plan	\$5m	\$0	\$5M	39.6%	\$1,752,207	\$3.25

## THE TAKEAWAY

The federal tax under Biden's proposed plan is almost double the capital gains tax that would have been due if the transaction occurred in 2021, prior to potential changes. **The buyer would have pocketed \$1m more if the transaction occurred before any tax changes.**

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## SOME STATES ARE ALSO PROPOSING TAX CHANGES

In addition to the deferral tax implications of the 2020 election, several states have proposed meaningful changes to their tax policy—including Washington, California and Colorado—which will add to the increased tax burden on transaction proceeds. The legislative landscape changes quickly - business owners thinking about short term exits should rely on professionals who are keeping close tabs on state regulations and tax changes that will impact these exits.

### WASHINGTONIANS: TAKE NOTE



Governor Inslee, as part of his 2021-2023 budget, has proposed a new 9% state tax on long-term capital gains to address significant state revenue shortfalls. Combined, with Biden's plans - **these two plans would more than double the amount of capital gains taxes a business owner may have to pay upon sale – effectively raising the base capital gains rate from 20% to 48.5%**. In short, these new proposals are potential game-changers for business owners who are developing exit strategies.

## WHAT TO DO?

### RECCOMENDATION

*“Given it can take 6-9 months or longer to complete the sale process, now is the time to engage and move forward.”*

While these changes have not yet taken effect, their potential impact on small to midsize business owners cannot be understated.

We recommend that business owners contemplating a sale seriously consider accelerating their timeline to avoid potentially significant tax impacts. Given it can take 6-9 months or longer to complete the sale process, now is the time to engage and move forward.

Moving faster now means a greater return on that most valuable asset - your business.



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Sources:

1. <https://taxfoundation.org/joe-biden-tax-plan-2020>
2. Capital gains tax proposal Q&A | Office of Financial Management (wa.gov) <https://bit.ly/2MQgBst>

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